paper through all the channels of commerce to protect it from alteration and forgery. And the relation of bank and customer does not ordinarily create any duty on the part of the customer to use any particular degree of care in drawing checks.[19]

Under the Negotiable Instruments Law, which has been adopted in almost all of the States, the rule of the law merchant—that an altered instrument is totally void—is changed, and the instrument is enforcible in the hands of a bona fide holder according to its original tenor, though not enforcible as altered.

FOLLOWING TRUST FUNDS.—The whole doctrine ot the tracing of trust funds is based upon the assumption that the trust fund can be identified, though possibly it does not remain in the hands of the trustee, and though it may have undergone several transmutations since the wrongful conversion.[1] To invoke this doctrine the *cestui* must be able to identify his property,[2] for as Blackstone says,[3] "It is a principle settled as far back as the time of the Year Books that, whatever alterations of form any property may undergo, the true owner is entitled to seize it in its new shape if he can prove the identity of the original material." Since it is often difficult to show the identity of the original property in its new form, the courts are very liberal in the sufficiency of identification required of the *cestui* to enable him to trace the trust fund.

Since money has no "earmarks," by which it can be identified, where the trust property consists of money, equity has established certain rules to enable the *cestui* to trace his property.[4] The importance to the *cestui* of tracing the trust funds is that he will be given preference over general creditors of the trustee, and equity will allow him to identify his property upon either one of two theories. The first one of these is that equity conclusively presumes that, although the trustee subsequently draws from his own funds with which are mixed the funds of the *cestui*, he has intended to draw from his own portion thereof rather than from that of the

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[19] Colonial Bank *v.* Marshall, *supra;* Worrell *v.* Gheen, *supra.*

[1] May *v.* Le Claire, 11 Wall. 217; United States *v.* State Bank, 96 U. S. 30.

[2] Primeau *v.* Granfield (C. C.), 184 Fed. 480; In re Mulligan, 116 Fed. 715; Farmers, etc., Bank *v.* King, 57 Pa. St. 202; Baker *v.* New York Bank, 100 N. Y. 31; Ferris *v.* Van Vechten, 73 N. Y. 113.

[3] 2 Bl. Comm. 405.

[4] In Massachusetts the doctrine long obtained that, since money has no "earmarks," there was no way to trace it after it became mingled with other money of the trustee. Howard *v.* Fay, 138 Mass. 104; White *v.* Chapin, 134 Mass. 230; Johnson *v.* Ames, 11 Pick. 173. While it is true that the exact coins or money of the *cestui* can not be identified, nevertheless equity enables the *cestui* to trace his money into the mingled fund and claim either a proportionate part of it or the property which it is invested in. See article by the late Dean Ames of the Harvard Law School, 19 HARV. LAW REV. 511.

cestui.[5] The second theory is that equity regards the mingled fund as charged with an equitable lien in favor of the *cestui* to the extent of his interest therein.[6]

It is clear that the first theory is a pure fiction of law, for it cannot be supposed that a trustee who had wrongfully converted a trust fund would really use his own funds before appropriating his ill-gotten gains. Nevertheless, as long as the total amount of the mingled fund does not fall below the amount of the cestui's interest, equity impresses a trust on the balance to the extent of the *cestui's* interest. However, when the balance falls below the amount of the *cestui's* interest, the trust fund is to the extent of the deficit, gone and no new deposits can revive it.[7] Some of the older cases, failing to recognize that this presumption of law was created solely to work out justice, have refused to extend it beyond actual fiduciaries, but by the overwhelming weight of authority the doctrine applies not only to ordinary trustees but also to constructive trustees.[8] Thus, equity will hold one to be constructive trustee who obtains the property of another by fraud, theft, conversion, etc., and the *cestui* can reclaim his property or the proceeds of it, provided he can identify it, using either of the two theories in the case where the trust property is money or has been converted into money.

The second theory is that equity will treat the mingled fund into which the money of the *cestui* has gone as charged with an

[5] Knatchbull *v.* Hallett, L. R. 13 Ch. Div. 696; National Bank *v.* Insurance Co., 104 U. S. 54; Elizalde *v.* Graves, 137 Cal. 634, 66 Pac. 369; Board of Commissioners *v.* Strawn, 157 Fed. 49, 84 C. C. A. 553, 15 L. R. A. (N. S.) 1100; Smith *v.* Mottley, 150 Fed. 266, 80 C. C. A. 154; Importers, etc., Bank *v.* Peters, 123 N. Y. 272.

[6] Peters *v.* Bain, 133 U. S. 670; National Bank *v.* Insurance Co., *supra;* Standard Oil Co. *v.* Hawkins, 74 Fed. 395, 20 C. C. A. 468; Peak *v.* Ellicott, 30 Kan. 156, 1 Pac. 499, 46 Am. Rep. 90; Davenport Plow Co. *v.* Lamp, 80 Iowa 722, 45 N. W. 1049; Englar *v.* Offcutt, 70 Md. 78. In the case of Frelinghuysen *v.* Nugent (C. C.), 36 Fed. 229, 239, the court said: "Formerly the equitable right of following misapplied money or other property into the hands of the parties receiving it, depended upon the ability of identifying it; the equity attaching only to the very property misapplied. This right was first extended to the proceeds of the property, namely, to that which was procured in place of it by exchange, purchase, or sale. But if it became confused with other property of the same kind, so as not to be distinguishable, without any fault on the part of the possessor, the equity was lost. Finally, however, it was held as the better doctrine that confusion does not destroy the equity entirely but converts it into a charge upon the entire mass, giving to the party injured by the unlawful diversion a priority of right over the other creditors."

[7] Merchantile Trust Co. *v.* St. Louis, etc., R. Co. (C. C.), 99 Fed. 485; Metropolitan Bank *v.* Campbell Commission Co. (C. C.), 77 Fed. 705; Spokane County *v.* First Nat. Bank, 68 Fed. 979, 16 C. C. A. 81; Boone County Nat. Bank *v.* Latimer (C. C.), 67 Fed. 27.

[8] Am. Sugar Refining Co. *v.* Fancher, 145 N. Y. 552; Converse *v.* Sickles, 146 N. Y. 200; Nat. Bank *v.* Barry, 125 Mass. 20; Bresniham *v.* Sheehan, 125 Mass. 11; United States *v.* State Bank, *supra;* Meader *v.* Norton, 11 Wall. 442; Richardson *v.* New Orleans, etc., Co., 102 Fed. 781, 42 C. C. A. 619; Standard Oil Co. *v.* Hawkins, *supra;* O'Neill *v.* O'Neill, 227 Pa. 334, 76 Atl. 26.

equitable lien in favor of the *cestui* to the extent of his interest, which lien attaches to the whole fund.[9] Under this theory the *cestui* may claim either what is left of the mingled fund, or he may claim property purchased with the fund or a part of it. It will therefore be seen that the rights of the *cestui* can be worked out much more completely under the lien theory than under the first theory. For example, let us suppose that a trustee mingles $100 of a trust fund with $100 of his own, and then draws out $100, with which he purchases property, and that subsequently he squanders the other $100. If it were conclusively presumed that the trustee first drew out his own fund, then there would be no property to which equity would attach a trust in favor of the *cestui*. But in this case equity does not apply the fiction, since it does not permit a wrong to be worked by legal presumptions.[10] But under the lien theory, the *cestui* has a choice of which he will take, the property bought or the remainder of the fund. Since the rest of the fund has been dissipated, the *cestui* would be able to take the property purchased. But under this theory, as under the first theory, if the total amount of the commingled fund at any time falls below the amount of the trust fund, to that extent the lien is gone so far as the mingled fund is concerned.[11] In the case of *In re A. O. Brown & Co.*,[12] in considering the rights of a claimant whose funds had been wrongfully mingled in a bank account with the funds of another, the court said:

> "All the deposits taken together constitute an obligation of the banker's, a single chose in action, amounting in total to the sum of the deposits. Upon that chose in action the beneficiary has a lien, if he wishes to assert it, equal to the sum of money which his property has contributed to it."

The right of a *cestui* to so trace his funds becomes of particular importance in transactions in which a bank on the verge of failure is concerned. Ordinarily the relation between a bank and its depositor is not a trust relation, but is simply that of debtor and creditor. Hence, generally, depositors must prove up along with other general creditors. But cases frequently arise where the circumstances indicate that the bank does not bear the relation of a simple contract debtor to third persons and equity in these cases will hold the bank to be a constructive trustee. Thus, where a bank receives a fund as agent to collect, or where it receives it knowing of the depositor's lack of title or authority to deposit, or where it receives it with knowledge of its impending insolvency, or in any other way through its own fraud, equity treats the bank as a con-

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[9] Cases cited *infra*, footnote 6. See also, 27 HARV. LAW REV. 125.

[10] In re Oatway, (1903) 2 Ch. 356.

[11] Whitcomb *v.* Carpenter, 134 Iowa 227, 111 N. W. 825, 10 L. R. A. (N. S.) 928; Massey *v.* Fisher (C. C.), 62 Fed. 958; Fisher *v.* Knight, 61 Fed. 491, 9 C. C. A. 582; People *v.* City Bank, 96 N. Y. 32; Farmers, etc., Bank *v.* King, 57 Pa. St. 202.

[12] 189 Fed. 432.

structive trustee, and the *cestui* is entitled to priority over general creditors, since under either of the two above theories he has traced his trust fund and identified it, provided the general balance of the bank has at no time fallen below the amount of his claim.[13]

In the recent case of *People* v. *California Safe Deposit Co.* (Cal.), 167 Pac. 388, the defendant bank sold to the petitioner some of the shares of its stock by means of fraudulent misrepresentations. As soon as the petitioner discovered the fraud, he rescinded the contract and sought to impress a trust in his favor on the deposits in the bank. At no time subsequent to the sale and prior to the closing of the bank did the deposits in the bank fall below the amount of the petitioner's claim. The court held that he was not entitled to a preference and must share *pari passu* with the general creditors. The court based its decision on the reasoning that a constructive trustee would not, in fact, draw from his own funds rather than from the trust fund, and it refused to allow a presumption that is in most cases contrary to fact. This holding appears to be out of line with the great weight of authority, for it is now settled that equity will conclusively presume that either the actual trustee or the constructive trustee has drawn from his own rather than from the trust funds. Under the lien theory no such presumption as this is necessary and the inconsistency of the other theory does not arise. However, the court did not apply the lien theory nor indicate in any way that such a theory exists.

[13] Woodhouse *v.* Crandall, 197 Ill. 104, 64 N. E. 292, 58 L. R. A. 385; Pennington *v.* Bank, 114 Va. 674, 77 S. E. 455; Western German Bank *v.* Norvell, 134 Fed. 724, 69 C. C. A. 330; Richardson *v.* New Orleans, etc., Co., *supra.* See LILE, NOTES ON EQ. JUR., p. 41 *et seq.*